DATE: August 10, 2016

TO: Open Space Board of Trustees

FROM: Peggy Bunzli, Executive Budget Officer
Devin Billingsley, Senior Budget Analyst
Eric Parish, Executive Vice President, MGT of America Consulting, LLC

SUBJECT: **2017 Budget Cost Allocation Plan**

Who is MGT?

MGT of America Consulting, LLC is a national public-sector consulting firm. The Financial Services division within MGT provides consulting services limited to cost allocation plan, user fee study and indirect cost rate calculation services exclusively for state and local governments. 36 MGT Financial Services consultants provide these services to over 100 state and local governments in Colorado and across the Country annually. Over the past five years MGT Financial Services consultants have completed over 500 engagements similar to the engagement completed for the City of Boulder.

Michelle Garrett, a Senior Consultant with MGT with over eight years of consulting experience, and Eric Parish, an Executive Vice President with MGT with over 25 years of consulting experience completed the past two cost allocation plans for the City of Boulder.

What is a cost allocation plan?

A cost allocation plan is an accounting document that identifies agency-wide indirect cost and allocates those costs to benefiting departments and funds.

This definition can be broken into three components. The first component is that the cost allocation plan is an accounting document. The cost plan is based on financial records, either actual expenditures or budgeted expenditures for a given fiscal year.

The second component is that the cost allocation plan identifies agency wide indirect costs. Indirect costs, in general terms, are costs found in departments that provide services to other departments. Those departments are mostly inward facing, with services benefiting other departments. Examples of areas of indirect costs at the department level include Human Resources, Information Technology and Accounting.

The third component is that the cost allocation plan distributes indirect costs to benefiting departments and funds.

The overall objectives of a cost allocation plan are to:

1. Identity the internal administrative and support departments
2. Document the costs of the internal administrative and support departments
3. Document the services provided by the internal administrative and support departments (e.g. payroll within Accounting or Help Desk with IT)
4. Distribute the internal administrative and support cost based on meaningful, measurable and auditable allocation bases or metrics to all departments and funds
5. Sum or total the administrative and support costs allocated to every department and fund.

What is the basis for a cost allocation plan?
The Federal Government provides principles and requirements to local governments for cost allocation plans. These requirements are found in The Code of Federal Regulations Part 200. (2 CFR Part 200). These requirements used to be found in OMB Circular A-87.

Additionally, cost allocation plans follow GAAP (Generally Accepted Accounting Principles) requirements and GFOA (Government Finance Officers Association) recommendations and best practices.

What cities and counties prepare a cost allocation plan?
Many cities and counties in Colorado and across the Country prepare cost allocation plans for internal and external purposes.

MGT prepares over 30 cost allocation plans for Colorado cities and counties annually including Boulder County, Denver and Colorado Springs.

Outside of Colorado MGT has recently prepared cost allocation plans for numerous jurisdictions including Houston, Dallas, Rockville, Oakland and Sacramento.

Why do cities and counties prepare a cost allocation plan?
There are numerous reasons that local governments prepare cost allocation plans. The first is to recover indirect costs on federal and state grants and awards. The cost allocation plan is the set of calculations to identify and document the cost of general fund administrative and support services provided to all operating departments. For certain grants and awards, this support, and the associated cost, can be reimbursed or recovered.

The second primary reason local governments prepare a cost allocation plan is to identify and document the general fund administrative and support services provided to non-general fund funds. In specific instances, this support, and the associated cost, can be reimbursed or recovered from enterprise and special revenue funds. In over simplified terms, the cost allocation plan is a single invoice for total services.

It is important to differentiate the terms “allocate” and “charge”. Every general fund operating department and non-general fund fund are “allocated” costs in the cost allocation plan. Not every operating general fund department and non-general fund fund is however, “charged”.

General fund operating departments are typically not “charged” their allocated costs. The costs allocated in the cost allocation plan are incurred by general fund departments. If for example, the jurisdiction “charged” the Police or Fire department, the city would have to appropriate additional general fund money to pay the allocated costs. This situation is essentially swirling the same general fund dollars.

However, it is common for Enterprise Funds and some special revenue funds to be “charged” for allocated costs. These funds either operate as a business with a unique customer base and revenue source or have characteristics that make it appropriate for these funds to actually pay for the administrative and support services they receive.

Should a local government choose not to charge an enterprise fund or certain special revenue fund for the administrative and supports services provided, then the jurisdiction is subsidizing those funds. The general fund is covering the administrative and support costs incurred by those enterprise and /or special revenue funds.

While these are the two most common reasons, local governments prepare cost allocation plans for other reasons as well.

What are details about the City of Boulder’s recent cost allocation plan?
The most recent cost allocation plan is based on the 2016 Budget (BY16). The most prior cost allocation plan was based on the Fiscal Year 2012 (FY12) actual expenditures. This is noteworthy for two reasons.

The first reason is the transition from actual costs to budget costs is not uncommon. Jurisdictions find that a cost plan based on actual costs represents, at best, at two-year lag between costs incurred and application in the budget process. This situation is not unique to the City of Boulder, it is universal because it is up to six months from the close of the fiscal year for actual audited expenditures to be available. Preparing the cost allocation plan can be another three months. At nine months into a fiscal year the current year budget will not be adjusted. The next window of opportunity to apply the recently completed cost allocation plan is the coming year. Therefore, the lag between results and application can be problematic.

The second reason is the gap between Boulder’s two most recent cost allocation plans is compounded due to the switch from actual to budget expenditures. Had the most recent cost allocation plan been prepared using actual expenditures instead of budget expenditures, the increase in allocated costs for all departments would be noticeable simply because of the normal increase in costs over this three year (FY12 to FY15) period of time. Since the recently completed cost allocation plan is based on BY16 expenditures, the time frame between cost allocation plans is actually four years not three (FY12 to BY16).

The costs that are allocated through the BY16 cost allocation plan have increased noticeably compared to the costs allocated through the last cost allocation plan based on FY12 actual expenditures. For example, allocable costs in the Finance department have increased approximately 29 percent over this time. Costs in City Manager's Office have increased approximately 63 percent over this time. Costs in the Human Resources have increased approximately 94 percent over this time.

The overall increase in allocated costs from the FY12 cost allocation plan to the BY16 cost allocation plan is approximately 28 percent from $22,374,000 to $28,543,000.

A material change occurred in the BY16 cost plan compared to the FY12 cost plan. The BY16 cost plan includes allowable costs for Property and Casualty insurance. These are allowable costs under both 2 CFR Part 200 and GAAP. These costs were not included in FY12 and earlier plans.

What are details about costs allocated to Open Space in the most recent cost allocation plan?
The costs allocated to Open Space in the BY16 cost allocation plan have increased approximately 25 percent compared to the FY12 cost allocation plan. This increase is less than the 28 percent increase in total costs allocated between the FY12 and BY16 cost allocation plans.

Comparable departments have increased allocations similar to Open Space. Planning increased approximately 20 percent and Recreation increased approximately 25 percent between the two cost plans.

In the BY16 cost allocation plan, of the total costs allocated to all city departments, approximately 6.67 percent are allocated to Open Space. Total costs allocated means the sum of the appropriate expenditures of the internal administrative and support departments. Flip the calculation around and approximately 93.33 percent of the total allocated costs are allocated to all other city general fund departments and restricted funds.

A common reasonableness check is to compare the total allocated costs to a department's share of total Full-Time Equivalent (FTE) employees. FTE is a basis for this test because many administrative and support services are labor driven. Meaning the more personnel a department has, will often result in the more services, and therefore costs, that the department receives.

Open Space has approximately 8.3 percent of the total city FTE count. Therefore, this ratio is within an expected range, 6.67 percent of allocated costs for 8.3 percent of the city FTE.

Another reasonableness test for allocated costs is the ratio of allocated costs to total expenditures for a department. This ratio for Open Space is approximately 5.5 percent. A common term across all sectors is “overhead rate”. Using this term, based on the BY16 cost allocation plan, the overhead rate for Open Space is 5.5 percent which falls well within a reasonable range.